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SUBJECT: Canada's 2010 Investment Climate Statement

A.1. Openness to Foreign Investment

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Strong economic fundamentals, proximity to the U.S. market, highly skilled employees, and abundant resources are key attractions for American investors in Canada. With few exceptions, Canada offers full national treatment to foreign investors within the context of a developed open market economy operating with democratic principles and institutions. Canada is, however, one of the few OECD countries that still has a formal investment review process. Foreign investment is also prohibited or restricted in several sectors of the economy.

Canada's economic development relies on foreign investment flows to a significant extent. The Canadian government estimates that foreign investors control about one quarter of Canada's nonfinancial corporate assets. The stock of global foreign direct investment in Canada stood at C$504.9 billion in 2008, an increase of 13.6 billion from 2007. U.S. investment accounted for 58 percent of the total (the same as 2007). However, for the first year ever Canadian direct investment to the United States exceeded US investment to Canada (by C$17.1 billion at the end of 2008).

The United States and Canada agree on important foreign investment principles, including right of establishment and national treatment. The 1989 Free Trade Agreement (FTA) recognized that a hospitable and secure investment climate is necessary to achieve the full benefits of reducing barriers to trade in goods and services. The FTA established a framework of investment principles sensitive to U.S. and Canadian interests while assuring that investment flowed freely between the two countries and investors were treated in a fair and equitable manner. The FTA provided higher review thresholds for U.S. investment in Canada than for other foreign investors, but the agreement did not exempt all American investment from review nor did the agreement override specific foreign investment prohibitions, notably in "cultural industries" (e.g., publishing, film, music).

The 1994 North American Free Trade Agreement (NAFTA) incorporated the gains made in the FTA, expanded the coverage of the Investment chapter to several new areas, and broadened the definition of investors' rights. The NAFTA also created the right to binding investor-state dispute settlement arbitration in specific situations.

-- Legal Framework: The Investment Canada Act

Since 1985, foreign investment policy in Canada has been guided by the Investment Canada Act (ICA), which replaced the more restrictive Foreign Investment Review Act. The ICA liberalized policy on foreign investment by recognizing that investment is central to economic growth and key to technological advancement. The ICA also provided for review of large acquisitions by non-Canadians and imposed a requirement that these investments be of "net benefit" to Canada. For the vast majority of small acquisitions, as well as the establishment of new businesses, foreign investors need only notify the Canadian government of their investment.

The threshold for investments subject to ICA review was increased in 2009 to C$312 million for WTO Members. (Indirect control acquisitions by WTO Members do not have to be reviewed.) For non-WTO Members, the threshold remains at C$5 million for direct control and C$50 million for indirect control acquisitions. From November 2008 to the end of October 2009, 371 foreign acquisitions were notified to Industry Canada, of which less than 10 percent were subject to review.

Investment in specific sectors is covered by the special

legislation. For example, foreign investment in the financial sector is administered by the federal Department of Finance Canada. Investment in any activity related to Canada's cultural heritage or national identity is administered by the Department of Canadian Heritage. Under provisions of Canada's Telecommunications Act, foreign ownership of transmission facilities is limited to 20 percent direct ownership and 33 percent through a holding company, for an effective limit of 46.7 percent total foreign ownership. The Broadcast Act governs foreign investment in radio and television broadcasting. (See below for more detail on these restrictions).

In addition to federal regulation, investment in Canada is also subject to provincial jurisdiction. Restrictions on foreign investment differ by province, but are largely confined to the purchase of land and to provincially regulated financial services. Provincial government policies relating to, inter alia, culture, language, labor relations or the environment, can be a factor for foreign investors.

U.S. foreign direct investment in Canada is subject to provisions of the Investment Canada Act, the WTO, and the NAFTA. Chapter 11 of the NAFTA ensures that future regulation of the U.S. investors in Canada (and Canadian investors in the United States) results in treatment no different than that extended to domestic investors within each country, i.e., "national treatment." Both governments are free to regulate the ongoing operation of business enterprises in their respective jurisdictions provided the governments accord national treatment to both U.S. and Canadian investors.

Existing U.S. and Canadian laws, policies, and practices were "grandfathered" under the NAFTA except where specific changes were required. The "grandfathering" froze various exceptions to national treatment provided in Canadian and U.S. law, such as foreign ownership restrictions in the communications and transportation industries The Canadian government retains the right to review the acquisition of firms in Canada by U.S. investors at the levels applicable to other WTO members and has required changes before approving some investments.

The U.S. and Canadian governments are free to tax foreign-owned companies on a different basis from domestic firms, provided this does not result in arbitrary or unjustifiable discrimination. The governments can also exempt the sale of Crown (government owned) corporations from any national treatment obligations. Finally, the two governments retain some flexibility in the application of national treatment obligations. They need not extend identical treatment, as long as the treatment is "equivalent."

-- Services Trade

Bilateral services trade is largely free of restrictions, and the NAFTA ensures that restrictions will not be applied in the future. However, preexisting restrictions, such as those in the financial sector, were not eliminated by the NAFTA. The NAFTA services agreement is primarily a code of principles that establishes national treatment, right of establishment, right of commercial presence, and transparency for a number of service sectors specifically enumerated in annexes to the NAFTA. The NAFTA also commits both governments to expand the list of covered service sectors (except for the financial services covered by NAFTA Chapter 14).

-- Federal Procurement

NAFTA grants U.S. firms that operate from the United States national treatment for most Canadian federal procurement opportunities. Interprovincial trade barriers, however, mean that U.S. firms established in one Canadian province can be prevented from bidding on another province's procurement opportunities. As a

first step in the ongoing and difficult process of reducing trade barriers within Canada, the Canadian federal, provincial, and territorial governments negotiated the Agreement on Internal Trade (AIT) that came into effect on July 1, 1995. The Agreement provides a framework for dealing with intra-Canada trade in ten specific sectors and establishes a formal process for resolving trade disputes. In January 2009, the provinces expanded the AIT to include improvements for labor mobility and dispute resolution.

In an attempt to further reduce interprovincial trade barriers, the provinces of British Columbia and Alberta signed a Trade, Investment, and Labor Mobility Agreement (TILMA) in 2006 to ensure that any provincial measures will not "operate to impair or restrict trade between or through the territory of the Parties, or investment or labor mobility between the Parties." The Agreement came into force in April 2009.

Besides the areas described above, the NAFTA includes provisions that enhance the ability of U.S. investors to enforce their rights through international arbitration; prohibit a broad range of performance requirements, including forced technology transfer, and expand coverage of the NAFTA investment chapter to include portfolio and intangible investments, as well as direct investment.

-- Investment in Cultural Industries

Canada defines cultural industries to include: the publication, distribution or sale of books, magazines, periodicals or newspapers, other than the sole activity of printing or typesetting; the production, distribution, sale or exhibition of

film or video recording, or audio or video music recordings; the publication, distribution or sale of music in print or machine-readable form; and any radio, television and cable television broadcasting undertakings and any satellite programming and broadcast network services.

The Investment Canada Act requires that foreign investment in the book publishing and distribution sector be compatible with Canadian national cultural policies and be of "net benefit" to Canada. Takeovers of Canadian-owned and controlled distribution businesses are not allowed. The establishment of new film distribution companies in Canada is permitted only for importation and distribution of proprietary products. Direct and indirect takeovers of foreign distribution businesses operating in Canada are permitted only if the investor undertakes to reinvest a portion of its Canadian earnings in Canada.

The Broadcasting Act sets out the policy objectives of enriching and strengthening the cultural, political, social, and economic fabric of Canada. The Canadian Radio-television and Telecommunications Commission (CRTC) administers broadcasting policy. Under current CRTC policy, in cases where a Canadian service is licensed in a format competitive with that of an authorized non-Canadian service, the commission can drop the non-Canadian service if a new Canadian applicant requests it to do so. Licenses will not be granted or renewed to firms that do not have at least 80 percent Canadian control, represented both by shareholding and by representation on the firms' board of directors.

While Canada allows up to 100 percent foreign equity in an enterprise to publish, distribute and sell periodicals, all foreign investments in this industry are subject to review by the Minister for Canadian Heritage, and investments may not occur through acquisition of a Canadian-owned enterprise. No more than 18 percent of the total advertising space in foreign periodicals exported to Canada may be aimed primarily at the Canadian market. Canadian advertisers may place advertisements in foreign-owned periodicals, and may claim a tax deduction for the advertising costs, including in cases where the periodical is a Canadian issue of foreign-owned periodical. One-half of advertising costs may be deducted in the case of publications with zero to 79 percent

original editorial content, and the full cost of advertising may be deducted in the case of publications with advertising may be deducted in the case of publications with 80 percent or more original editorial content.

This regime is the result of a 1999 agreement between the United States and Canada, which balanced U.S. publishers' desire for access to the Canadian market against Canada's desire to ensure that Canadian advertising expenditures support the production of Canadian editorial content.

-- Investment in the Financial Sector

Canada is open to foreign investment in the banking, insurance, and securities brokerage sectors, but there are barriers to foreign investment in retail banking. Foreign financial firms interested in investing submit their applications to the Office of the Superintendent of Financial Institutions (OSFI) for approval by the Minister of Finance. U.S. firms are present in all three sectors, but play secondary roles. Canadian banks have been much more aggressive in entering the U.S. retail banking market because there are no barriers that limit access. Although U.S. and other foreign banks have long been able to establish banking subsidiaries in

Canada, no U.S. banks have retail banking operations in Canada, which is regarded as a fairly "saturated" market. Several U.S. financial institutions have established branches in Canada, chiefly targeting commercial lending, investment banking, and niche markets such as credit card issuance.

Chapter 14 of the NAFTA deals specifically with the financial services sector, and eliminates discriminatory asset and capital restrictions on U.S. bank subsidiaries in Canada. The NAFTA also exempts U.S. firms and investors from the federal "10/25" rule so that they will be treated the same as Canadian firms. The "10/25" rule prevents any non-NAFTA, nonresident entity from acquiring more than ten percent of the shares (and all such entities collectively from acquiring more than 25 percent of the shares) of a federally regulated, Canadian-controlled financial institution. In 2001, the Canadian government raised the ten percent limit for single, non-NAFTA shareholders to 20 percent. Several provinces, however, including Ontario and Quebec, have similar "10/25" rules for provincially chartered trust and insurance companies that were not waived under the NAFTA.

-- Investment in Other Sectors

Commercial Aviation: Currently Canada limits foreign ownership of Canadian air carriers to 25 percent of voting equity. In addition, foreigners may own nonvoting equity subject to the overall requirement that they are not permitted to control a Canadian air carrier. The recently signed Canada-EU Aviation Agreement envisions changes to Canadian legislation that will allow up to a 49 percent foreign stake in Canadian airlines; but this will require action by the parliament and no specific date for the new limits to come into force have been announced.

General Aviation: No non-Canadian (other than permanent residents) may register a general aviation aircraft for commercial or personal use in Canada.

Energy and Mining: Generally foreigners cannot be majority owners of uranium mines.

Telecommunications: Under provisions of Canada's Telecommunications Act, direct foreign ownership of Type 1 carriers

(owners/operators of transmission facilities) is limited to 20 percent. Ownership and control rules are more flexible for holding companies that wish to invest in Canadian carriers. Under these

rules, two thirds of the holding company's equity must be owned and controlled by Canadians.

Fishing: Foreigners can own up to 49 percent of companies that hold Canadian commercial fishing licenses.

Electric Power Generation and Distribution: Regulatory reform in electricity continues in Canada in expectation that increased competition will lower costs of electricity supply. Province-owned power firms are also interested in gaining greater access to the U.S. power market. Since power markets fall under the competency of the Canadian provinces, they are at the forefront of the reform effort. The reforms will also help to further integrate the U.S. and Canadian electricity markets.

Real Estate: Primary responsibility for property law rests with the provinces. Prince Edward Island, Saskatchewan, and Nova Scotia all limit real estate sales to out-of-province parties. There is no constitutional protection for property rights in Canada. Consequently, government authorities can expropriate property after paying appropriate compensation.

Privatization: Federal and provincial privatizations are considered on a case-by-case basis, and there are no overall limitations with regard to foreign ownership. As an example, the federal Department of Transport did not impose any limitations in the 1995 privatization of Canadian National Railway, whose majority shareholders are now U.S. persons.

-- Investment Incentives

Federal and provincial governments in Canada offer a wide array of investment incentives that municipalities are generally prohibited from doing. None of the federal incentives are specifically aimed at promoting or discouraging foreign investment in Canada. The incentives are designed to advance broader policy goals, such as boosting research and development or promoting regional economies. The funds are available to any qualified Canadian or foreign investor who agrees to use the monies for the stated purpose. For example, Export Development Canada can support inbound investment under certain specific conditions (e.g., investment must be export-focused; export contracts must be in hand or companies have a track record; there is a world or regional product mandate for the product to be produced).

Provincial incentives tend to be more investor-specific and are conditioned on applying the funds to an investment in the granting province. Provincial incentives may also be restricted to firms established in the province or that agree to establish a facility in the province. Government officials at both the federal and provincial levels expect investors who receive investment incentives to use them for the agreed purpose, but no enforcement mechanism exists.

Incentives for investment in cultural industries, at both the federal and provincial level, are generally available only to Canadian-controlled firms. Incentives may take the form of grants, loans, loan guarantees, venture capital, or tax credits. Incentive programs in Canada generally are not oriented toward export promotion. Provincial incentive programs for film production in Canada are available to foreign filmmakers.

-- Canada's Ranking in Selected Business Indices

Index

Year

Metric

Ranking

TI Corruption Index

2009

CPI Score 8.7

8

Heritage Economic Freedom

2009

Overall Score 80.5

7

WB Ease of Doing Business

2009

8

(MCC Indices Not Applicable)

A.2. Conversion and Transfer Policies

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The Canadian dollar is fully convertible. The Canadian government provides some incentives for Canadian investment in developing countries through Canadian International Development Agency (CIDA) programs. Canada's official export credit agency, the Export Development Corporation (EDC), provides political risk insurance to Canadian companies with investments in foreign countries and to lenders who finance transactions pursued by Canadian companies abroad.

A.3. Expropriation and Compensation

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Canadian federal and provincial laws recognize both the right of the government to expropriate private property for a public purpose, and the obligation to pay compensation. The federal government has not nationalized any foreign firm since the nationalization of Axis property during World War II. Both the federal and provincial governments have assumed control of private firms usually financially distressed ones after reaching agreement with the former owners. In December 2008, the province of Newfoundland and Labrador acted to take control of assets relating to a U.S. company's operations in the province. The action raised questions as to whether the province was expropriating rights and assets of the company - possibly without compensation.

A.4. Dispute Settlement

Canada is a member of the New York Convention of 1958 on the Recognition and Enforcement of Foreign Arbitral Awards. The

Canadian government has made a decision in principle to become a member of the international Center for the Settlement of Investment Disputes (ICSID). However, since the ICSID legal enforcement mechanism requires provincial legislation, the federal government must also obtain agreement from the provinces that they will enforce ICSID decisions. Although most provinces have endorsed the agreement, full agreement is unlikely in the foreseeable future.

Canada accepts binding arbitration of investment disputes to which it is a party only when it has specifically agreed to do so through a bilateral or multilateral agreement, such as a Foreign Investment Protection Agreement (see below). The provisions of Chapter 11 of the NAFTA guide the resolution of investment disputes between NAFTA persons and the NAFTA member governments. The NAFTA encourages parties to settle disputes through consultation or negotiation. It also establishes special arbitration procedures for investment disputes, separate from arbitration procedures, for investment disputes separate from the NAFTA's general dispute settlement provisions.

Under the NAFTA, a narrow range of disputes dealing with government monopolies and expropriation between an investor from a NAFTA country and a NAFTA government may be settled, at the investor's option, by binding international arbitration. An investor who seeks binding arbitration in a dispute with a NAFTA party gives up his right to seek redress through the court system of the NAFTA party, except for proceedings seeking nonmonetary damages.

A.5. Performance Requirements and Incentives

The NAFTA prohibits the United States or Canada from imposing export or domestic content performance requirements, and Canada does not explicitly negotiate performance requirements with foreign investors. For investments subject to review, however, the investor's intentions regarding employment, resource processing, domestic content, exports, and technology development or transfer can be examined by the Canadian government. Investment reviews often lead to negotiation of a package of specific "undertakings," such as agreement to promote Canadian products. In 2009, the Government of Canada filed a suit in the Canadian courts against U.S. Steel alleging that the company had failed to fulfill its undertaking to maintain minimum employment levels in exchange for permission to acquire a Canadian steel mill.

A.6. Right to Private Ownership and Establishment

Investors have full rights to private ownership.

A.7. Protection of Property Rights

Foreigner investors have full and fair access to Canada's legal system, with private property right limited only by the rights of governments to establish monopolies and to expropriate for public purposes. Investors from NAFTA countries have mechanisms available

to them for dispute resolution regarding property expropriation by the Government of Canada.

Canada has yet to ratify key treaties that protect copyright works on the Internet (the World Intellectual Property Organization) (WIPO) "Internet Treaties") that the government signed in 1997. Refer to the copyright section of this report for more details. U. ¶S. (and many Canadian) companies have complained that Canada's enforcement regime against counterfeiting and piracy, both at the border and internally, is cumbersome and ineffective and further hampered law enforcement officials' legal restrictions from sharing information with rights holders.

A.8 Transparency of the Regulatory System

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The transparency of Canada's regulatory system is similar to that of the United States. Proposed legislation is subject to parliamentary debate and public hearings, and regulations are issued in draft form for public comment prior to implementation. While federal and/or provincial licenses or permits may be needed to engage in economic activities, regulation of these activities is generally for statistical or tax compliance reasons. The Bureau of Competition Policy and the Competition Tribunal, a quasi -judicial body, enforce Canada's antitrust legislation.

A.9. Efficient Capital Markets and Portfolio Investment

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Canada's capital markets are open, accessible, and without onerous regulatory requirements. Foreign investors are able to get credit in the local market. In 2008 and 2009, the World Economic Forum and Moody's Investor Service ranked Canada's banking system as the "most sound" in the world, and first in the world for financial strength, respectively. Canadian banking stability is linked to high capitalization rates that are well above the norms set by the Bank for International Settlements.

The Canadian banking industry includes 22 domestic banks, 26 foreign bank subsidiaries and 22 full-service foreign bank branches and seven foreign bank lending branches operating in Canada. In total, these institutions manage close to C$2.9 trillion in assets. Many large international banks have a presence in Canada through a subsidiary, representative office or branch of the parent bank.

In Canada, the regulation of defensive tactics against hostile takeovers is handled by provincial securities regulators rather than the courts. Canadian regulators have adopted a National Policy regarding takeovers that seeks to encourage open and unrestricted auctions to maximize target company shareholder value and choice between competing alternatives. The nationality of the bidding entity is not considered by the provincial securities

regulators but trigger a federal review under the Investment Canada Act.

While cross-shareholding arrangements are permitted in Canada, the extent of foreign investment and cross-border M&A activity suggests that they do not pose any practical barriers.

A.10. Competition from State-Owned Enterprises

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Canada has around 100 state-owned enterprises (SOEs), however the vast majority of assets are held by four federal crown corporations: Canada Mortgage and Housing Corporation; Farm Credit Canada; Business Development Bank of Canada; and Export Development Canada. The Treasury Board Secretariat provides an annual report to Parliament regarding the governance and performance of Canada's crown corporations and other corporate interests.

There are no restrictions on the ability of private enterprises to compete with SOEs. However, the functions of most Canadian crown corporations have limited appeal to the private sector, e.g. the Canadian Space Agency. However, the activities of some SOEs such as VIA Rail and Canada Post do overlap with private enterprise. As such, they are subject to the rules of the Competition Act to prevent abuse of dominance and other anti-competitive practices. Foreign investors are also able to challenge SOEs under the NAFTA and WTO.

Canada does not have a sovereign wealth fund but the province of Alberta has the Heritage Savings Trust Fund established through province's share of petroleum royalties. The fund's value was approximately C$15 billion in 2009. It is invested in a globally diversified portfolio of public and private equity, fixed income and real assets.

A.11. Corporate Social Responsibility

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The Government of Canada encourages Canadian companies to observe the OECD Guidelines for Multinational Enterprises in their operations abroad and provides a National Contact Point for dealing with issues that arise in relation to Canadian companies. Despite the increased level of official attention paid to CSR, the activities of Canadian mining companies abroad remain the subject of critical attention and have prompted calls for the government to move beyond voluntary measures.

A.12. Political Violence

Political violence occurs in Canada to about the same extent as in the United States. For example, protest at the North American Leaders, Summit in Montebello, QC in August 2007 led to confrontation between police and protesters.

A.13. Corruption

On an international scale, corruption in Canada is low and similar to that found in the United States. In general, the type of due diligence that would be required in the United States to avoid corrupt practices would be appropriate in Canada. Canada is a party to the UN Convention Against Corruption. Canada is also a party to the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, as well as the

Inter-American Convention Against Corruption.

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A.14. Bilateral Investment Treaties

While the terms of the FTA and NAFTA guide investment relations between Canada and the United States, Canada has also negotiated international investment agreements with non-NAFTA parties. These agreements, known as Foreign Investment Protection Agreements (FIPAs), are bilateral treaties that promote and protect foreign investment through a system of legally binding rights and obligation based on the same principles found in the NAFTA. Canada has negotiated FIPAs with countries in Central Europe, Latin America, Africa, and Asia, and has over 100 international tax treaties in force.

A.15. OPIC and Other Investment Insurance Programs

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Because Canada is a developed country, the U.S. Overseas Private Investment Corporation does not operate in Canada.

A.16. Labor

The federal government and provincial/territorial governments share jurisdiction for labor regulation and standards. Federal employees and those employed in the railroad, airline, and banking sector are covered under the federally administered Canada Labor Code. Employees in most other sectors come under provincial labor codes. As the laws vary somewhat from one jurisdiction to another, it is advisable to contact a federal or provincial labor office for specifics, such as minimum wage and benefit requirements. The global economic crisis of 2008-2009 was accompanied by job loss across the country, particularly in manufacturing and construction. Canada's unemployment rate stood at 8.5 percent at the end of 2009,

up from years of relative stability between 6 and 6.5 percent.

Figures for 2008 show the proportion of union membership among those in paid, nonagricultural employment at 29.4 percent. Overall union membership reflected a 16.3 percent unionized rate in the private sector and a 71 percent unionized rate in the public sector.

A.17. Foreign Trade Zones/Free Ports

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Under the NAFTA, Canada operated as a free trade zone for products made in the United States. U.S. made goods enter Canada duty free.

A.18. Foreign Direct Investment Statistics

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The United States has long been Canada's top target for foreign investment, and Canada is the third largest recipient of U.S. direct investment after the United Kingdom and the Netherlands. About 58 percent of Canada's foreign direct investment comes from the United States. At the end of 2008, Canada hosted some C$293.6 billion in U.S. direct foreign investment abroad. U.S. investors with large direct investments in Canada include major automakers (GM, Ford, Chrysler), integrated energy, chemical and mineral producers (e.g., ExxonMobil, ChevronTexaco, ConocoPhillips), financial services firms (e.g., Citibank), and retailers (e.g., Wal-Mart). In terms of inward FDI performance, Canada attracted 3.2 per cent of the world's FDI in 2008 and accounted for 1.9 per cent of world GDP.

Canadian residents have become increasingly active as worldwide investors, and their net international liabilities have been shrinking over the past decade relative to national income. The United States is the top destination for Canadian foreign direct investment. In 2008, with total investment around C$310 billion, Canada took the top spot as the largest source of FDI to the United States. Other major destinations for Canadian FDI are the United Kingdom, other European Union countries, Brazil, Australia and Chile.
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